

7 IN THE UNITED STATES DISTRICT COURT
8 FOR THE DISTRICT OF ARIZONA
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12 Cordelia SMITH,)
13 Plaintiff,) No. CIV 01-2182 PHX RCB
14 vs.) ORDER
15 ALLSTATE INSURANCE COMPANY,)
16 Defendant.)
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18 Plaintiff Cordelia Smith filed this lawsuit in Arizona
19 Superior Court on October 9, 2001. On November 8, 2001 Defendant
20 Allstate filed a notice of removal with this Court (doc. # 1)
21 claiming federal diversity jurisdiction pursuant to 28 U.S.C. §
22 1332. Thereafter, Allstate filed a motion to dismiss for failure
23 to state a claim (doc. # 2). Smith then filed a motion to remand
24 the action to state court (doc. # 4). In the event the Court does
25 not grant remand, Smith has asked the Court to certify the
26 underlying legal question of Allstate's duty to Smith to the
27 Arizona Supreme Court (doc. #5). The Court heard oral argument in
28 . . .

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1 this matter on February 4, 2002 and now rules.¹

2 I. Background

3 Smith and her husband were insured under an automobile
4 insurance policy issued by Allstate. Allstate's Notice of Removal
5 (doc. # 1) Ex. 1 at ¶ III. On December 31, 1995, Smith was riding
6 in a vehicle driven by her husband when he entered the intersection
7 of Grand Avenue and 15th Avenue in Phoenix against a red light and
8 collided with another vehicle. Id. Smith suffered personal
9 injuries as a result of the accident and her husband's negligence.
10 Id. at ¶¶ III-IV.

11 Allstate offered Smith \$30,000 to settle her claim, which was
12 refused. Id. at ¶ IV. The case was then taken to arbitration and
13 Smith was awarded \$144,310. Id. Allstate appealed the arbitration
14 award. Id. Smith then brought suit against her husband in state
15 court. Id. After a trial, the jury awarded Smith damages in the
16 amount of \$240,000. Id. Allstate paid the judgment in January,
17 2000. Id. Smith is now suing Allstate for breach of the covenant
18 of good faith and fair dealing. Id. at ¶ V.

19 II. Remand

20 Allstate removed this action to federal court on the basis of
21 diversity jurisdiction, pursuant to 28 U.S.C. § 1441. Smith now
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23 ¹On February 4, 2002, the day oral argument was held on
24 Defendant's motion to dismiss, Plaintiff filed an Amended Complaint
25 pursuant to Rule 15 of the Federal Rules of Civil Procedure.
26 Plaintiff continues to assert the same theories advanced in the
27 original Complaint, but adds a theory of assignment of any bad
28 faith claim Plaintiff's husband may have had against Defendants.
This last theory was not and could not be part of the motion to
dismiss now pending before the Court. Therefore, this Order is
directed to the original Complaint and the Amended Complaint in so
far as it asserts theories of liability on the basis of Plaintiff's
personal bad faith claim against Defendant.

1 moves to remand the case based on a lack of diversity of
2 citizenship. The statute governing remand states: "If at any time
3 before final judgment it appears that the district court lacks
4 subject matter jurisdiction, the case shall be remanded." 28
5 U.S.C. § 1447(c).

6 Smith is a citizen of Arizona. Allstate's Notice of Removal
7 (doc. #1) Ex. 1 at ¶ I. Smith argues that jurisdiction does not
8 exist because Allstate is also considered a citizen of Arizona for
9 purposes of this lawsuit. She argues that the exception under 28
10 U.S.C. § 1332(C)(1) applies. That statute states: " . . . in any
11 direct action against the insurer of a policy or contract of
12 liability insurance, . . . to which action the insured is not
13 joined as a party-defendant, such insurer shall be deemed a citizen
14 of the State of which the insured is a citizen," 28
15 U.S.C. § 1332(C)(1). Allstate contends that a bad faith claim is
16 not a direct action; therefore the § 1332(C)(1) exception does not
17 apply. In the absence of the exception Allstate is a citizen of
18 the state of its incorporation and its principal place of business,
19 both of which are Illinois, and diversity jurisdiction is proper.
20 Allstate's Notice of Removal (doc. # 1) at 2.

21 Smith's arguments against jurisdiction lack merit. The Ninth
22 Circuit has held that "a bad faith action brought by an insured
23 against the insurer is not a 'direct action' within the meaning of
24 28 U.S.C. § 1332(c)(1). Rather, a direct action is one in which a
25 plaintiff is entitled to bring suit against the tortfeasor's
26 liability insurer without joining the insured." Searles v.
27 Cincinnati Ins. Co., 998 F.2d 728, 730 (9th Cir. 1993).

28 There is no collateral estoppel against Allstate as Smith

1 claims. The Ninth Circuit has held that the case cited by Smith,
2 Chavarria v. Allstate Ins. Co., 749 F. Supp. 220 (C.D. Cal. 1990),
3 was wrongly decided and has since discredited it. Searles, 998
4 F.2d at 728-29. As such, it would be inappropriate to attach any
5 preclusive effect to the Chavarria court's determination. See
6 Restatement (Second) of Judgments § 28(2). Additionally, Allstate
7 has not admitted that this case is a direct action by citing
8 General Accident Fire & Life Insurance Corp. v. Little, 103 Ariz.
9 435, 443 P.2d 690 (1968), in its motion to dismiss. That case did
10 not address whether a bad faith claim is a direct action and it was
11 not cited by Allstate for any such proposition.

12 Finally, Smith's contention that this case does not embody the
13 purpose and spirit of the diversity jurisdiction statute while
14 fulfilling its technical requirements is a legislative and not a
15 legal argument. The jurisdiction of this Court has been properly
16 invoked under § 1332, and as such the Court has an obligation to
17 exercise it. First State Ins. Co. v. Callan Assoc., Inc., 113 F.3d
18 161, 163 (9th Cir. 1997).

19 III. Certification to State Supreme Court

20 Allstate has moved to dismiss Smith's claim because Allstate
21 insists that it had no duty of good faith toward Smith for a claim
22 based on her husband's negligence. Smith has asked that this Court
23 certify the question of Allstate's duty to the Arizona Supreme
24 Court because there is no controlling precedent in Arizona.

25 The Court has discretion to make a decision or certify the
26 question to the state supreme court. See White v. Celotex Corp.,
27 907 F.2d 104, 106 (9th Cir. 1990). If the Court chooses to rule it
28 "must predict how the highest state court would decide the issue

1 using intermediate appellate court decisions, decisions from other
2 jurisdictions, statutes, treatises, and restatements as guidance."
3 Arizona Elec. Power Coop. v. Berkeley, 59 F.3d 988, 991 (9th Cir.
4 1995). Therefore, the Court looks to factors such as the
5 complexity of the issue, the availability of precedent from lower
6 courts or other jurisdictions, and the magnitude of disagreement on
7 the issue to determine whether certification is appropriate. See
8 id.; Rigden v. United States, 995 F. 2d 727, 735 n.6 (9th Cir.
9 1986).

10 In this case, certification is not necessary. The issue of
11 Allstate's duty is not complex. The Court is not required to wade
12 into any intricate or abstruse administrative or statutory scheme.
13 The scope of an insurer's duty of good faith can be defined by
14 reference to well-established common law principles. Furthermore,
15 while there are no cases in Arizona and few precedents from other
16 jurisdictions that address this issue, the decisions that do
17 address this issue appear to be nearly uniform—indicating a lack of
18 serious debate. See Sperry v. Sperry, 990 P.2d 381 (Utah 1999);
19 Herrig v. Herrig, 844 P.2d 487 (Wyo. 1992); Rumley v. Allstate
20 Indem. Co., 924 S.W.2d 448 (Tex. Ct. App. 1996); Wilson v. Wilson,
21 468 S.E.2d 495 (N.C. App. 1996); but see Decroli, (1988). Given
22 these circumstances the Court will deny Smith's motion.

23 IV. Motion to Dismiss

24 Allstate moves to dismiss Smith's bad faith claim pursuant to
25 Rule 12(b)(6) of the Federal Rules of Civil Procedure. Allstate
26 argues that Smith cannot assert a bad faith claim because insurers
27 have no duty of good faith to third parties. Although Smith was a
28 co-insured under the policy, Allstate contends that she stood in

1 the position of a third-party claimant in seeking damages for her
2 husband's negligence.

3 An insurance company's duty of good faith and fair dealing
4 exists only between the insurer and its insured. An insurance
5 company owes no duty of good faith to a third-party claimant. Leal
6 v. Allstate Insurance Co., 199 Ariz. 250, 17 P.3d 95 (2000). The
7 question raised by the instant action is whether an insured should
8 be considered a third-party claimant when she is injured by a
9 coinsured's negligence and she claims liability benefits under a
10 jointly owned insurance policy.

11 As discussed previously, there are no Arizona cases addressing
12 this issue. Four jurisdictions have dealt with this question
13 directly, in factual circumstances nearly identical to this case.
14 All four jurisdictions held that an insured is a third-party
15 claimant when seeking benefits based on a co-insured's liability
16 coverage. Sperry v. Sperry, 990 P.2d 381 (Utah 1999); Herrig v.
17 Herrig, 844 P.2d 487 (Wyo. 1992); Rumley v. Allstate Indem. Co.,
18 924 S.W.2d 448 (Tex. Ct. App. 1996); Wilson v. Wilson, 468 S.E.2d
19 495 (N.C. App. 1996).

20 One reason for treating the co-insured as a third-party
21 claimant is because the coverage is transaction specific. Sperry,
22 990 P.2d at 384; Rumley, 924 S.W.2d at 450. In the situation
23 where, as here, a person sues because of the negligence of her
24 spouse, she is seeking benefits based on her husband's coverage and
25 not her own. Sperry, 990 P.2d at 384. Her position is that of an
26 antagonist rather than a co-claimant. 924 S.W.2d at 450. As such,
27 she relates to the insurer as a third-party, and it is reasonable
28 that the insurer would respond likewise. Herrig, 844 P.2d at 491;

1 Wilson, 468 S.E.2d at 498-99.

2 Another justification for treating a coinsured as a third-
3 party is the conflict of interest that would otherwise be created
4 for the insurance company. This conflict would compromise the
5 insurer's ability to protect the interests of its insured because
6 the insurer would owe an equal yet inconsistent duty to each party.
7 Sperry, 990 P.2d at 384; Herrig, 844 P.2d at 491-91. It would also
8 "make any such insurer an almost certain target for a claim of
9 breach of one of these duties, in addition to the claim for the
10 underlying negligence." Sperry, 990 P.2d at 384.

11 Finally, the contractual relationship between an insurance
12 company and an insured does not implicate the duty to act in good
13 faith in all situations. In a case where the claimant and the
14 insured hold separate insurance policies with the same insurer the
15 insurance company does not owe a duty to both. Rumley, 924 S.W.2d
16 at 449. "In these cases, the courts almost universally hold that
17 the insurer does not owe a duty of good faith and fair dealing to
18 the injured party when he asserts a third-party claim against
19 another of the insurer's insureds." Herrig, 844 P.2d at 491.

20 The one case to the contrary held that an insurer owed a duty
21 of good faith to a claimant where that insurer had affirmatively
22 assumed a position of trust with the claimant by promising to
23 assist with her claims. That insurer's duty, however, only
24 extended to informing the claimant of her right to seek benefit's
25 under her co-insured's liability coverage and advising her to
26 obtain independent counsel. Dercoli v. Pennsylvania Nat'l Mut.
27 Ins. Co., 554 A.2d 906 (Penn. 1989). The rule from this case has
28 been rejected by the Arizona Supreme Court. Leal v. Allstate Ins.

1 Co., 199 Ariz. 250, 17 P.3d 95 (2000).

2 Smith offers three arguments in support of her position that
3 Arizona would allow a bad faith claim to go forward in the present
4 situation.² Smith contends that liability under an insurance
5 contract can only be limited by specific language, and no language
6 in Smith's policy limited Allstate's duty of good faith. Smith's
7 argument presupposes that the duty of good faith runs to an insured
8 regardless of circumstance. This is clearly not true. If both the
9 claimant and negligent party were insured by Allstate under
10 separate policies, Allstate would have no duty of good faith to the
11 claimant regardless of contract language. See Fobes v. Blue Cross
12 & Blue Shield of Ariz., Inc., 176 Ariz. 407, 861 P.2d 692 (1993).

13 This is true because good faith is a legal duty overlaid upon on a
14 contractual relationship. Therefore, while the existence of a
15 contractual relationship is a prerequisite to an insurer's duty of
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18 ²At oral argument Plaintiff's attorney raised, for the first
19 time, the argument that insurance premiums paid from community
20 property create a duty of good faith toward the marital community.
21 The Court does not believe this argument makes a difference in the
22 analysis of Plaintiff's individual claims against Defendant. To
23 the extent that it would change the Court's analysis, Plaintiff's
24 argument contradicts established Arizona case law. For example, in
25 Fobes v. Blue Cross & Blue Shield, 861 P.2d 692 (Ariz. Ct. App.
26 1993), the Arizona Court of Appeals held that an insurance company
27 had no duty of good faith to the wife of an insured when they were
28 covered under separate policies, even though the premiums were paid
from community property and the medical expenses incurred by the
husband were community debts. Plaintiff's argument would dictate
the opposite result. If an insurance company owes a duty to the
marital community, rather than the individual insured, then the
wife in Fobes would have been allowed to sue the insurance company
for a breach of good faith as a type of third-party beneficiary to
the insurance contract, even though she and her husband held
separate insurance policies. However, the Fobes court determined
that the wife did not enjoy any species of third-party beneficiary
status under her husband's policy based on a community property
argument. Fobes, 861 P.2d at 696.

1 good faith, the contract does not define its scope. Deese v. State
2 Farm Mut. Auto. Ins. Co., 172 Ariz. 504, 508, 838 P.2d 1265, 1269
3 (1982). Moreover, accepting Smith's argument would recognize a
4 dangerous precedent. If insurance companies were allowed to limit
5 or abolish their duty of good faith by contract language they most
6 certainly would do so; then no insured would be protected.

7 Next Smith contends that treating her as a stranger to the
8 insurance contract deprives her of the security she purchased. She
9 contends that she has paid premiums to Allstate since approximately
10 1980 for this security. This argument, however, does not address
11 the fact that the security interest she purchased was for her
12 coverage and not necessarily her husband's. Smith points to
13 nothing in her contractual relationship with Allstate that suggests
14 she purchased an added measure of security when suing another of
15 Allstate's insureds, even a joint policy holder. Therefore,
16 treating her as a third-party claimant does not deprive her of any
17 security guaranteed under her contract with Allstate.

18 Smith further asserts that the conflict of interest created by
19 imposing a duty of good faith on Allstate when suing a co-insured
20 under the policy is not a significant problem. She maintains that
21 for decades insurance carriers have maintained an "absolute right
22 to take conflicting positions" under Arizona law. Opposition to
23 Mot. to Dismiss (doc. # 6) at 3. The only case she cites to
24 support this averment is United Servs. Auto. Ass'n v. Morris, 154
25 Ariz. 113, 741 P.2d 246 (1987). In Morris, an insurance company
26 wanted to have complete control over settlement while reserving the
27 right to contest coverage. Id. at 251. Recognizing the strong
28 conflict between the insurer's interests and the insured's, and the

1 high potential for abuse if either had absolute control, the
2 Arizona Supreme Court determined that where an insurance company
3 reserves the right to contest coverage the insured has a right to
4 decide whether to accept or reject a settlement offer. Id. at 254.
5 Thus, if Morris is applicable at all to this situation, it is
6 because this case demonstrates that an insurance company does not
7 have an absolute right to take conflicting positions. If an
8 insurer chooses to take a position that may put it at odds with the
9 insured's interest then the insurer's right to act for the insured
10 will be correspondingly diminished. This case strongly suggests
11 that the Arizona Supreme Court would not be inclined to adopt
12 Plaintiff's rule, which would purposely create a direct conflict
13 of interest between insurers and their insureds.

14 The Court is convinced that the Arizona Supreme Court would
15 follow the nearly unanimous precedent from other jurisdictions and
16 hold that an individual is a third-party claimant when she is
17 injured by a co-insured's negligence and she claims liability
18 benefits under a jointly owned insurance policy. The reasoning of
19 these cases are sound and certainly applicable to the present
20 situation. Additionally, Smith has not demonstrated that any law
21 or policy in Arizona would dictate a different result.

22 Thus, in conclusion the Court will deny Plaintiff's motion for
23 remand because the Court has diversity jurisdiction. The Court
24 will also deny Plaintiff's request for certification of the
25 question of an insurer's duty to a joint policy holder to the State
26 Supreme Court because the issue is not complex and there is a lack
27 of serious debate. Finally, the Court will grant Defendant's
28 motion to dismiss Plaintiff's individual claims because an insurer

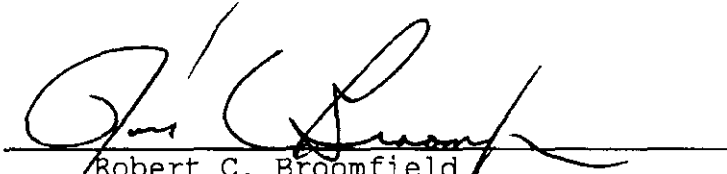
1 owes no duty of good faith to a joint policy holder who claims
2 benefits under the joint insured's liability coverage, thereby
3 standing in the position of a third-party claimant. Any theory of
4 liability set out in the Amended Complaint that is based on an
5 assignment of the husband's rights against the insurance company
6 for an alleged breach of the duty of good faith remains.

7 IT IS ORDERED that Plaintiff's Motion to Remand (doc. # 4) is
8 DENIED.

9 IT IS FURTHER ORDERED that Plaintiff's Request (Motion) to
10 Consider Certification of Question to State Court (doc. # 5) is
11 DENIED.

12 IT IS FURTHER ORDERED that Defendant's Motion to Dismiss (doc.
13 # 2) is GRANTED.

14 DATED this 13 day of February, 2002.

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18 Robert C. Broomfield
Senior United States District Judge

19 Copies to counsel of record
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